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An AICPA publication for the local firm

HOW TO IMPROVE YOUR BOTTOM LINE

For several years now there has been an ongoing series of events, both inside and outside the profession, that affect firms' financial results. Despite current difficulties, I believe the future is extremely bright for local firms. At Metcalf, Zima & Company, we have developed a long-range plan that projects what our firm will be doing in the year 2000. We believe that conditions in the years ahead will provide opportunities to bring new services to local practices. What we local practitioners have to do, though, is examine our whole fee-generating process and turn these opportunities into bottom-line results.

What does it take to make more profit?

The initial step in improving firm profitability is to look at your service potential. To do this, I suggest you use the T-account (the accounting equation) approach. It is a simple system, but one that works.

First, list as assets all of the services you are currently providing. Then, find out what services other practitioners in your service area are selling. List as a liability any service that you are not providing. You then want to see if you can develop any of these services in your own firm. If you can turn the liabilities into assets, the net result is equity.

You need talent in the firm in order to develop new services. Personnel can be evaluated using the same T-account method. List people's positive characteristics and abilities as assets and their weaknesses as liabilities. (The knowledge and skill form in section 307.02 of the AICPA *MAP Handbook* can be helpful in this regard.) Work on eliminating the liabilities. Help your staff to improve. Create personal equity for all staff members, and their talent will help you grow.

Small firms might consider developing niches and specialties. One promising area, I believe, is servicing the legal profession.

At Metcalf, Zima & Company, we subscribe to a program called Services to the Legal Profession, which is a service provided by Hudson Sawyer. We are provided with a quarterly newsletter, the *Law Management Journal*, which we send to law firms. The program also provides marketing brochures, and a six-part course on law firm management that our staff presents to law firms. We were also trained in legal profession issues as part of the package.

The new business we are seeing from this program convinces us that we made the best decision. The opportunities are immense. We are becoming heavily involved in litigation support and expert testimony and we are expanding our tax practice with the growth in the legal niche. The referrals which come from attorneys lead to more profitable work, and we find that our staff enjoys the reputation as *the* CPA firm serving attorneys in Atlanta. The firms subscribing to this program in other cities are experiencing the same success.

There are two other areas where involvement can be beneficial—in state society activities and in your local community. It is important to stay current regarding professional issues. Serving on state society committees keeps you informed about professional developments and also gives your firm visibility.

Think politically. Assume a leadership role in community affairs. We CPAs are trained to analyze and solve problems. If things aren't going right in your community, it provides you with a tremendous opportunity to offer help and become known. Become campaign chairman for a charitable organ-

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ization, for example. It will open doors for you and can lead to your making a significant number of contacts.

Budgeting and planning

Manage your practice from the bottom line up. That is, determine the bottom-line results you want, and budget accordingly. When drawing up a long-range plan, it is sometimes difficult to get all partners to understand what you are trying to achieve. They might not like some of the interim results. A better way to budget is to have partners determine what they want to earn, and then determine the chargeable hours needed at the realization rate you can expect—that's your net fee goal.

Long-range planning is more than a numbers process, however. It involves many steps, among which the most important is identifying the firm's purpose—its philosophy. You must decide what you want the firm to be.

As part of our long-range plan for the year 2000, we have a picture in front of us of the volume we will be doing, the annual percentage increase in chargeable hours that this will require, and the number of partners in the firm and what their average income will be. We also have a picture of the makeup of our staff and the type of facility we will own. Probably 60 percent of the staff will be women, and we envision having a day-care center so that we can attract and retain top talent in our firm.

In short, write down what you want your firm to be five to ten years in the future, and put a picture in front of your partners. Create a profile of the firm you want. The numbers, then, are easy.

Regarding the firm's financial and organizational structure, think cash. Measure your successes and failures in cash. Determine where you are making money and where you are not. And don't give one person the sole responsibility for managing the firm. By all means, have a managing partner, but also have a management committee. If you are a sole practitioner, get an outsider, such as a banker, involved. (You and the banker can be an advisory board.) You need a balance in every firm.

Broadcast your plan. Involve all members of the firm in it. If you let people know what your plan is, they will help you achieve it. Go over the financial results with the staff. If you are a sole proprietor, go over the results with an outside advisor.

You can also use your long-range plan when recruiting. Give your plan and financial results to the accounting professors at one or two schools. Let them know what you are trying to accomplish. Show them that you can offer opportunities, and encourage them to send you talented students. Don't pass up recruiting as a means of building. It is expensive, but it is also an investment in the future.

Several state societies have "résumé banks" of trained staff, for both the use of member firms and their clients who are looking for controllers. It is also well worth considering part-time paraprofessionals. We have found them to be most productive, very profitable, and businesslike. The staff in our client write-up department, for example, has a realization rate of over 100 percent. Administrative personnel are important to firms. Tell them about your plans. They need to be inspired, too.

Expense control

Our largest and most manageable expense is people. We need to increase staff members' utilization rates. Delegate more, instruct better, and set a good example. If we do that, we will find that their realization rates can increase, too.

Utilization involves weeding out clients who don't suit your practice. You can spend a lot of time with clients who are not profitable for your firm. Such clients may pay poorly; that is, they may pay late or argue about fees, they may have low realization rates, or their work may expose you to risks without rewards.

Most often, your staff's time can be better spent. By decreasing your people cost, your staff becomes more vital to your success. In summary, I believe in the future of public accounting. We just have to make sure we are making money at what we are doing. ☑

—by **Donald P. Zima, CPA,** *Metcalf, Zima & Company, 1700 Peachtree Summit, 401 West Peachtree Street, Atlanta, Georgia 30308*

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Highlights of Recent Pronouncements

FASB Statement of Financial Accounting Standards

No. 102 (February 1989), *Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale*

- ☐ Amends FASB Statement no. 95, *Statement of Cash Flows,* to exempt the following from the requirement to provide a statement of cash flows:
  1) Defined benefit pension plans covered by FASB Statement no. 35, *Accounting and Reporting by Defined Benefit Pension Plans,* and certain other employee benefit plans.
  2) Highly liquid investment companies that meet specified conditions.
- ☐ Requires that cash receipts and cash payments resulting from acquisitions and sales of the following be classified as operating cash flows in a statement of cash flows:
  1) Securities and other assets that are acquired specifically for resale and are carried at market value in a trading account.
  2) Loans that are acquired specifically for resale and are carried at market value or the lower of cost or market value.
- ☐ Effective for financial statements issued after February 28, 1989, with earlier application encouraged.

Statements on Auditing Standards

No. 61 (April 1988), *Communication with Audit Committees*

- ☐ Requires the auditor to determine that certain matters related to the conduct of an audit are communicated, either in writing or orally, to those having responsibility for oversight of the financial reporting process.
- ☐ Applicable to entities that have either an audit committee or other formally designated group equivalent to an audit committee, and to all Securities and Exchange Commission engagements.
- ☐ Requires the auditor to ensure that the audit committee receives additional information regarding the scope and results of the audit that may assist them in overseeing the financial reporting and disclosure process.
- ☐ Effective for audits of financial statements for periods beginning on or after January 1, 1989. Earlier application is permissible.

No. 60 (April 1988), *Communication of Internal Control Structure Related Matters Noted in an Audit*

- ☐ Supersedes SAS no. 20, *Required Communication of Material Weaknesses in Internal Control.*
- ☐ Supersedes SAS no. 30, *Reporting on Internal Accounting Control,* paragraphs 47-53.
- ☐ Provides guidance in identifying and communicating conditions that relate to an entity's internal control structure observed during an audit of financial statements.
- ☐ Defines items to be communicated as "reportable conditions" which are significant deficiencies in the internal control structure.
- ☐ Provides guidance on establishing, between auditor and client, agreed-upon criteria for identifying and reporting additional matters.
- ☐ Effective for audits of financial statements for periods beginning on or after January 1, 1989. Earlier application is permissible.

No. 59 (April 1988), *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*

- ☐ Supersedes SAS no. 34, *The Auditor's Considerations When a Question Arises About an Entity's Continued Existence.*
- ☐ Provides guidance in conducting an audit of financial statements in accordance with GAAS with respect to evaluating whether there is substantial doubt about the entity's ability to continue as a going concern.
- ☐ Effective for audits of financial statements for periods beginning on or after January 1, 1989. Earlier application is permissible.

No. 58 (April 1988), *Reports on Audited Financial Statements*

- ☐ Supersedes:
  1) SAS no. 1, section 546, *Reporting on Inconsistency,* section 545, *Inadequate Disclosure,* and section 542, *Other Conditions Which Preclude the Application of Necessary Auditing Procedures.*
  2) SAS no. 2, *Reports on Audited Financial Statements.*
  3) SAS no. 15, *Reports on Comparative Financial Statements.*
- ☐ Prescribes a new form for the auditor's standard report, including:
  1) The addition of an introductory paragraph that differentiates management's responsibilities for the financial statements from the auditor's role in expressing an opinion on them.
  2) An explicit acknowledgment that an audit provides reasonable assurance within the context of materiality.

3) The addition of a brief explanation of what an audit entails.

☐ Revises the second standard of reporting to require a reference to consistency in the auditor's report only when accounting principles have not been consistently applied.

☐ Changes the manner of reporting on material uncertainty to eliminate the "subject to" opinion qualification while retaining the requirement to discuss the matter.

☐ Expands the guidance for addressing and evaluating uncertainties.

☐ Effective for reports issued or reissued on or after January 1, 1989. Earlier application is permissible.

No. 57 (April 1988), *Auditing Accounting Estimates*

☐ Provides guidance to auditors on obtaining and evaluating sufficient competent evidence to support significant accounting estimates in an audit.

☐ Defines an accounting estimate as an approximation of financial statement element, item, or account.

☐ Effective for audits of financial statements for periods beginning on or after January 1, 1989. Earlier application is permissible.

No. 56 (April 1988), *Analytical Procedures*

☐ Supersedes SAS no. 23, *Analytical Review Procedures.*

☐ Provides guidance on and requires the use of analytical procedures in the planning and overall review stages of all audits.

☐ Provides guidance on the use of analytical procedures as substantive tests.

☐ Effective for audits of financial statements for periods beginning on or after January 1, 1989. Earlier application is permissible.

Quality Review

Standards for Performing and Reporting on Quality Reviews (March 1989)

☐ Provides the standards for performing and reporting on all reviews conducted under the AICPA quality review program.

☐ Applicable to firms enrolled in the AICPA quality review program, to individuals and firms who perform and report on such reviews, to state CPA societies that participate in the administration of the program, to associations of CPA firms that assist their members in arranging and carrying out quality reviews, and to the AICPA Quality Review Division.

Information for Members

Technical information

The primary responsibility of the twelve people who staff the Institute's technical information service is to answer members' questions on technical matters. They receive some 48,000 inquiries per year on accounting principles, financial statement presentation, auditing and reporting standards, and certain aspects of professional practice, excluding tax and legal matters. If you would like some assistance, we encourage you to call toll-free: United States, (800) 223-4158; New York State, (800) 522-5430.

Library services

The AICPA library's staff can offer assistance on a broad range of business topics. AICPA members anywhere in the U.S. may borrow from the library's extensive collection. For assistance, just call these toll-free numbers: United States, (800) 223-4155; New York State, (800) 522-5434.

Please note that toll-free calls cannot be transferred to other Institute departments.

Total On-Line Tax and Accounting Library (TOTAL)
NAARS accounting and financial data library

Subscribers have access to different types of files in the Institute's NAARS library. These are corporate and local governmental annual reports, including financial statements, footnotes, auditors' opinions, and all current and superseded authoritative and semi-authoritative literature from the AICPA, FASB, GASB, and SEC. TOTAL subscribers can also access tax and other information. For further information, just call Hal Clark: (212) 575-6393.

Know Your PC

How do you know when you buy microcomputer equipment that you are getting what was specified on the purchase contract? There have been instances, for example, where the internal hard disks installed were not the ones ordered, resulting in much slower machines and other problems. If the software is disk-intensive, where the program calls information from the disk and writes information to it quite often, as many desktop publishing and database management programs do, the difference in response time can be significant, and the computer may malfunction.

In these instances, the first step is to learn how the machine is configured, that is, to find out just what hardware it contains. One could open the case to look, but for a nontechnical person using either an IBM or compatible computer, a better solution would be a utility program, such as Norton Utilities Advanced Edition, which is available for under $100 from Peter Norton Computing, 2210 Wilshire Boulevard, Suite 186, Santa Monica, California 90403-5784.

The major thrust of this program is to unerase files. Those who wonder what is inside their computers will be interested in another utility it offers called Speed Index.

I ran Speed Index (SI C:) on my equipment as an example. Here's what appeared on the monitor:

```
c:\si c:
SI-System Information, Advanced Edition, (c) Copr 1987, Peter Norton
        Computer Name: Epson Equity
     Operating System: DOS 3.30
       Main Processor: Intel 80286                  Serial Ports: 1
         Co-Processor: None                       Parallel Ports: 1
Video Display Adapter: Enhanced Graphics, 256 K-bytes
   Current Video Mode: Text, 80 x 25 Color
Available Disk Drives: 4, A: - D:

DOS reports 640 K-bytes of memory:
168 K-bytes used by DOS and resident programs
472 K-bytes available for application programs
A search for active memory finds:
640 K-bytes main memory      (at hex 0000-A000)
32 K-bytes display memory    (at hex B800-C000)
ROM-BIOS Extensions are found at hex paragraphs: C000

Computing Index (CI), relative to IBM/XT: 11.7
Disk Index (DI), relative to IBM/XT: 2.8

Performance Index (PI), relative to IBM/XT: 8.7
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The indexes are positioned with the 8088-based IBM PC XT which has the value of 1.0. The Epson Equity II+ uses a quartz clock that moves data at 12 megahertz (MHz) or 12 million times a second, while the XT runs at 4.77 MHz. Because of design elements, the computing index for the Epsom is 11.7, almost 12 times that of the XT.

When a hard disk is used, the read/write head moves at random to gather or store data. The speed for this random-access read or write on the hard disk in the Epson is about 28 milliseconds, while the read/write speed in the original XT ran at some 80 milliseconds. Thus, the disk index in this unit is 2.8 (80 divided by 28). The program factored the computing index with the disk index and rated the machine's performance index at 8.7 relative to the XT. That is, the Epson should perform almost nine times faster than the XT.

An example of this utility's usefulness was at a firm that uses a Compaq 286 with a 20 megabyte hard disk and a laser printer to publish a variety of documents. The operator, a graphic artist, found that files became lost and documents, garbled.

When Speed Index was run on the Compaq, it showed the disk index to be 1.1—much slower than it should have been. With the 10 MHz chip, the computing index was about 9.7. The performance index calculated to approximately 2.3 (about twice as fast as an XT). The low disk index reading meant that either the hard disk was defective or of lower quality than the one ordered.

It turned out that the customer, wanting immediate delivery, had agreed to have a slower hard disk installed until a faster one became available. Somehow, the upgrade had never been made, and the graphic artist lacked the technical expertise to realize the computer wasn't operating up to par.

Running Speed Index on the upgraded machine revealed that the computing index remained at 9.7, but that the disk index had increased to 2.8. As a result, the overall performance index climbed to about 5.9. The faster hard disk had increased the machine's performance from a little more than double to almost six times that of the XT.

How much difference does this make? Well, a task that could take fifteen minutes for the 80-millisecond unit to complete, might take the 28-millisecond hard disk about five minutes. In addition, the operator of the malfunctioning Compaq computer reports that since updating the hard disk, the other problems seemed to have cleared up as well. ☑

—by **Dale Archibald,** *P. O. Box 6573, Minneapolis, Minnesota 55406, tel. (612) 724-8917*

1989 AICPA National Practice Management Conferences

The AICPA management of an accounting practice committee offers two programs this year that are targeted specifically to the managing partners of local firms. Both conferences feature presentations, panel responses, small group discussions, question-and-answer periods, and an optional evening discussion session.

MAP West on July 24-26 at the Sheraton Hotel and Towers, Seattle, Washington

Topics include: boosting productivity and profitability; institutionalizing the firm for greater efficiency; organizing your firm for marketing; what the managing partner should know about upcoming computer technology; what a regional firm looks for in a merger candidate; high performance management; improving the quality of work life; coping with partner separation; effective time management; finding future firm leaders; and leverage through effective delegation.

MAP East on October 23-25 held at the Waverly Hotel, Atlanta, Georgia

Topics include: the leadership skills necessary for dynamic management; professional management in a CPA firm; managing today's staff; conflict management; legal issues in managing firm employees; merging your firm for growth; improving the quality of work life; what has happened to firm profits; quality service through financial graphics; matrix management (who does what in the local firm); and how to slice the pie—a look at partners' compensation.

For further information about the conferences, contact the AICPA industry and practice management division: (212) 575-3814.

Partner Retirement/Buy-out

How can you avoid "My Client" syndrome, and get partners to turn clients over to other partners? How do you avoid client loss after partner retirement? Is two years before a partner retires too short a time to begin a double-partner approach to client retention? These are some of the questions asked at MAP conferences by practitioners. Other requests are for methods or techniques for buying out a partner on retirement, and suggestions on factoring retirement into current compensation. We asked our editorial advisers for their suggestions.

Sidney F. Jarrow, who practices in Elmhurst, Illinois, says that one way to avoid the "My Client" syndrome is to have a strong managing partner who has the authority to make changes. Mr. Jarrow thinks that a double-partner approach can help in this regard, as well as in client retention. He says that two years is too short a time and believes five to ten years before a partner's retirement might not be too soon in certain instances.

Other practitioners think that two years is too long a period, however. David A. Werbelow, a Pasadena, California, practitioner, suggests one year. Also, he thinks that loss of clients after a partner's retirement can be avoided by reducing retirement benefits for any clients "taken."

Robert L. Israeloff, who practices in Valley Stream, New York, believes that client loss can be avoided after a partner retires by planning and reassigning in advance. "We assign clients of a retiring partner approximately six months before a partner actually retires," he says. Mr. Israeloff thinks that two years is far too long a time frame. "It is not practical," he says. "There is too much wasted time, and I don't believe anything is really accomplished."

As for buying out a partner on retirement, Mr. Israeloff says, "Our firm pays the retiring partner his total income for the last three years over a ten-year period."

Richard A. Berenson, a New York City practitioner, also believes that two years is too long for a double-partner approach. He says it would be too expensive because the client can obviously only be billed for the services of one partner.

Mr. Berenson says that a retiring partner should receive his proportionate share of accrual book value and some payment for firm goodwill. "This usually results in an accrual capital payout over a one-year period, and a goodwill payout equal to three years' income paid over ten years," he adds.

A larger issue not addressed, according to Mr. Berenson, is whether this retirement should be funded out of current earnings, thereby having the retiring partner participate in his own retirement funding, or whether the retirement should be funded only after a partner retires.

Avoiding the "My Client" syndrome simply requires constant attention, according to H.W. Martin, a retired Rome, Georgia, CPA. Mr. Martin suggests this can be indirectly tied in with the partners' retirement provision in the partnership agreement. He says that if the agreement provides for payment to the former partner only for accounts that are kept by the firm, partners having the "I" complex should be able to recognize that the firm concept of "We," "Us," and "Our" will pay him handsomely. "Regardless of the financial rewards, some people apparently need the 'I' for their egos, so endless correction is necessary," he adds.

Regarding turning over accounts, Mr. Martin says that you cannot expect a partner to turn accounts over so long as the individual can properly handle his work load. When he cannot, then the time has come to transfer accounts to other partners; gener-

1989 AICPA National Small Firm Conference

A new format at this year's conference will enable participants to attend two general sessions—management techniques for the small firm, and leadership, power, and productivity—and to select from concurrent workshops. These half-day programs will offer presentations and discussions, and opportunities to tackle case studies and practice management questions on success strategies for the sole practitioner, the selection and evaluation of partners, financial administration, and the skills necessary to hire and motivate good staff.

Optional evening sessions include open practice management forums and "30-Minute MAP"—informal minipresentations on marketing techniques for getting clients, gearing up to merge, how firms can use desktop publishing, getting ready for quality review, preparing a personnel guide for your firm, structuring a partner buy-out, time and billing software, and whether you need a firm administrator.

The Small Firm Conference will be held on two dates in two different locations:

August 23-24	**November 9-10**
Westin Hotel,	**Pointe at Tapatio Cliffs,**
Chicago, Illinois	**Phoenix, Arizona**

For further information, contact the AICPA industry and practice management division: (212) 575-3814. ☑

ally, the transferring partner will welcome the help.

Mr. Martin says that firms should not lose clients upon the retirement of a partner, if a proper and timely transfer to the remaining partners is made. All partners should be involved in making the plan, and when the plan is adopted, it should be reduced to writing so everyone can fully understand it and, of course, have a copy.

Mr. Martin suggests that a complete list of the retiring partner's accounts should be made and proposed succeeding partners' names inserted. The list should be broken down between major clients, smaller clients, and the run-of-the-mill personal tax returns, because each requires a different changeover time. Large accounts should be transferred as much as five years before retirement (with both partners being engaged for at least two of those years). The smaller accounts (principally compilations and reviews) should work out well with a year advance timing, and run-of-the-mill personal tax returns turned over the last year before retirement.

Another suggestion is that the retiring partner should visit each client (except the small tax returns) to discuss his retirement. If the client does not have a choice for the successor partner, then the name that the firm has selected should be offered. The client should have full right of choice.

He thinks that the small tax returns may involve so many clients that it is not feasible to contact them, but rather suggests waiting for them to call to make an appointment to have their returns prepared. Then, the matter of retirement can be brought up and a successor selected by the client. Both the retiring and successor partners should meet with the client when he brings in his information, and the retiring partner should make sure the successor is familiar with the return and the client's problems.

Mr. Martin thinks that this joint interview is essential to convince the client that the successor is familiar with his work, and that he or she is being well-served. He says these small accounts are sometimes harder to transfer than the larger ones, but he successfully transferred 484 small returns this way on his own retirement.

As a retiring partner transfers his work, this will leave time to do other things in the office, such as cleaning up the odds and ends in his practice and performing nonrecurring jobs for other partners. Lastly, he should review all of his clients' files to determine that the working papers are in good order for his successor. Mr. Martin cautions that it is both time-consuming and tedious to transfer the accounts from a large practice, but says it will pay off if handled properly. ☑

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